

Office of Chief Counsel
Internal Revenue Service
memorandum

CC:WR:PNW:SEA:TL-N-97-99
TNTomashek

Date: FEB 11 1999
To: District Director, Seattle
Attn: Chuck Heino, Group Manager MS W131
From: District Counsel, Seattle MS 670

Subject: Request for Advisory Opinion
Taxpayer: [REDACTED]

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Collection, Criminal Investigations, Examination or Appeals, recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Collection, Criminal Investigations, Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

This refers to Revenue Agent Danny L. LaTurner's memorandum of December 17, 1998, supplemented by your routing slips of January 5 and 29, 1999, requesting our advice in the above-entitled case.

ISSUE

The issue is whether the taxpayer is entitled to defer prepaid subscription amounts under I.R.C. § 455 where the taxpayer did not make a timely election as required by § 455(c).

FACTUAL BACKGROUND

[REDACTED], an accrual basis taxpayer, first began receiving subscription income from the sale of [REDACTED] during the taxable year ended [REDACTED], which currently is under

010770

examination. On its corporate income tax return for that period, and for each succeeding year, the taxpayer reported the subscription income using the deferral method allowed by § 455. The taxpayer never has formally elected the deferral method as required by the code and regulations.

LEGAL DISCUSSION

As a general rule, a taxpayer is required to include gross income in the year of receipt and may not defer it to a later year unless such deferral is specifically authorized by statute. I.R.C. § 451; American Automobile Association v. United States, 367 U.S. 687 (1961); Schlude v. Commissioner, 372 U.S. 128 (1963). Section 455 provides a statutory exception to the general rule for prepaid subscription income.

A taxpayer must elect to defer the reporting of income under § 455. If the required election is not made, then the prepaid subscription income must be included in gross income for the taxable year in which it is received. Treas. Reg. § 1.455-1.

The election may be made without the consent of the Service for a taxpayer's "first taxable year in which he receives prepaid subscription income . . . ," but must be made no later than the time for filing the income tax return for such year. I.R.C. § 455(c)(3)(B). The election is to be made by means of a statement attached to the return. Treas. Reg. § 1.455-6(a)(1).

Treas. Reg. § 1.455-6(a)(2) provides as follows:

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Collection, Criminal Investigations, Examination or Appeals, recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Collection, Criminal Investigations, Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

"The statement shall indicate that the taxpayer is electing to apply the provisions of section 455 to his trade or business, and shall contain the following information:

- (i) The name and a description of the taxpayer's trade or business to which the election is to apply;
- (ii) The method of accounting used in such trade or business;
- (iii) The total amount of prepaid subscription income from such trade or business for the taxable year;
- (iv) The period or periods over which the liability of the taxpayer to furnish or deliver a newspaper, magazine, or other periodical extends;
- (v) The amount of prepaid subscription income applicable to each such period; and
- (vi) A description of the method used in allocating the prepaid subscription income to each such period."

Under Treas. Reg. § 1.455-6(b), if a taxpayer seeks to make the election after the due date of the return for the first taxable year in which he receives prepaid subscription income, he must obtain the consent of the Service. In either case, the election must contain the information listed above.

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Collection, Criminal Investigations, Examination or Appeals, recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Collection, Criminal Investigations, Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

It is clear that the taxpayer in this case, cannot qualify for deferral of its prepaid subscription income on the basis of having made the election as required by the code and regulations, because it did not make the election. However, that is not the end of the inquiry. It is necessary for the Service to inspect the taxpayer's income tax return for the period ending [REDACTED], to determine whether it contains the information required to be included in the statement described in Treas. Reg. § 1.455-6(a)(2)(i) through (vi). If the information is present, then the taxpayer could argue that the return contains an effective election under § 455 by virtue of the "substantial compliance" doctrine.

The substantial compliance doctrine has been applied by courts in order to find that, in certain narrow circumstances, a tax election is valid because the taxpayer has substantially complied with the procedures for making the election. Prussner v. United States, 896 F.2d 218 (7th Cir. 1990); Fischer Industries Inc. v. Commissioner, 87 T.C. 116 (1986). It is noteworthy in applying this doctrine that a taxpayer's mere use of an accounting method accurately on the tax return does not constitute substantial compliance with the requirements for making an election. Knight-Ridder Newspapers v. United States, 743 F.2d 781 (11th Cir. 1984). Please see Letter Ruling 9846001 (July 2, 1998), copy enclosed.

Even if the taxpayer has not substantially complied with the election requirements under § 455 by including the information listed in Treas. Reg. § 1.455-6(a)(2)(i) through (vi), the possibility of relief under § 301.9100-3 of the Procedure and Administration Regulations must be considered. The procedure for a taxpayer to

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Collection, Criminal Investigations, Examination or Appeals, recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Collection, Criminal Investigations, Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

follow in requesting relief under this provision is set forth in section 5.02 of Rev. Proc. 99-1, 1999-1 I.R.B. 6 (January 4, 1999). We suggest that you contact Industry Specialist Art Lucchese (Media/Communications) at (708) 743-0581 for further information regarding this aspect of the case.

CONCLUSION

The taxpayer must comply with the election requirements of Code section 455 and the regulations thereunder in order to qualify for the deferral of prepaid subscription income, and [REDACTED] has not done so. However, an inspection of the income tax return for the first year in which the taxpayer received prepaid subscription income will be necessary to determine whether the taxpayer has substantially complied with the regulations by including the necessary information. Furthermore, even if there has not been substantial compliance with the regulations, there is a possibility that the taxpayer could obtain relief under Treas. Reg. § 301.9100-3.

If you need any further assistance in this case, please do not hesitate to call on us. We are closing our file subject to reopening if the need arises. If you have any questions regarding this matter, please contact the undersigned at (206) 220-5951.

IS/TNT

THOMAS N. TOMASHEK
Special Litigation Assistant

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Collection, Criminal Investigations, Examination or Appeals, recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Collection, Criminal Investigations, Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.